INDEX

CITATIONS

704064—46

In the Supreme Court of the United States

OCTOBER TERM, 1946

No. 268

O. WILLIAM LOWRY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The majority and dissenting opinions in the Tax Court (R. 191–201) are reported at 3 T. C. 730. The opinion of the Circuit Court of Appeals (R. 222–225) is reported at 154 F. 2d 448.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on April 3, 1946. (R. 221.) The petition for a writ of certiorari was filed on July 3, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether family-partnership income credited on the books to petitioner's wife was properly taxed to the petitioner, under Section 22 (a), Internal Revenue Code.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> (26 U. S. C., Sec. 22.)

STATEMENT

The Tax Court's findings of fact (R. 181–190) may be summarized as follows:

By January, 1937, O. William Lowry, the petitioner, and Charles R. Sligh, Jr., owned equally all of the capital stock of the Charles R. Sligh Company, which manufactured and sold furniture and allied products. (R. 181.) In the spring of 1937 they felt that corporate taxes were "a drain

on the business and prevented its growth" and they discussed with their tax consultant and their attorney the advisability of forming a partnership with their wives. On May 24, 1937, Lowry transferred one-half of his shares to his wife. (R. 182.) In the spring of 1938 Lowry and Sligh again considered liquidating the corporation and forming a partnership to carry on the business. They discussed the matter on numerous occasions with their banker, tax consultant, insurance agent and attorney. They were advised by their tax consultant to wait until December, 1938, before making the move. On December 1, 1938, Sligh transferred one-half of his shares of stock to his wife. (R. 183.) On December 10, 1938, a plan for the complete liquidation of the corporation was adopted by the stockholders. (R. 183.) On December 15, 1938, all of the corporation's assets were distributed, subject to all liabilities, in redemption of all of the outstanding stock and in complete liquidation of the corporation. A limited partnership agreement was executed on December 16, 1938, designating Lowry and Sligh as general partners and their wives as limited partners. On the same day the four individuals executed a bill of sale conveying the machinery, furniture, inventories, and all tangible property, and interests in all intangible property to the general partners. On the previous day the land upon which the plant was

situated and two leases had been conveyed by the corporation directly to the general partners pursuant to directions of its stockholders. (R. 184.)

The limited partnership agreement provided, in part, that the limited partnership should exist for a term of five years, subject to extension at the option of the general partners; that the business shall be of the same nature as before, but that the general partners may engage in any other business without the consent of the limited partners; that the profits, after allowing for salaries to the general partners and others items, are to be divided into four parts but that no profits shall be distributed until the general partners so decide; that the limited partners are not personally liable for any losses of the firm and they are to be held harmless from liability for any of the liabilities of the corporation assumed by the partnership; that the value of the corporate assets transferred to the partnership shall be fixed by the general partners but these values are not conclusive as to the value of the interest of any partners upon the dissolution of the firm for any cause; and that neither the general nor the limited partners shall have the right to withdraw capital contributions. Upon dissolution, the limited partners had no right to demand property other than cash. Management and control of the business was solely in the hands of the general

partners. (R. 185–188.) The wives performed no services. (R. 190.)

For the partnership's first fiscal period, December 16, 1938, to May 31, 1939, its income tax return allocated $2,226.08 of net income to Mrs. Sligh and $2,226.07 to Mrs. Lowry. The partnership return for the fiscal year ending May 31, 1940, allocated $11,095.29 each to Mrs. Lowry and Mrs. Sligh. (R. 189.) Neither of the wives withdrew any money during the period ending May 31, 1939. During the period ending May 31, 1940, Mrs. Sligh's withdrawal account was charged $718.37 to pay her income tax. During the same period Mrs. Lowry's account was charged $1,309.56, of which about $500 was for the purchase of an automobile and the balance was for the payment of income tax. (R. 190.)

The Commissioner included in the incomes of Messrs. Lowry and Sligh for 1939 and 1940 the amounts reported by their respective wives as their shares of partnership income. The deficiency notice stated that this action was taken because the wives rendered no services and contributed no capital, as such, to the business and because each husband, in the close family group, retained dominion, control, and administration of the business. (R. 190.)

The Tax Court found that Messrs. Lowry and Sligh did not relinquish dominion and control over any part of the assets in the corporation by

reason of the gifts of stock in the corporation to their wives and consequently that the wives did not contribute any property to the capital of the partnership. (R. 190.) It held that Messrs. Lowry and Sligh were each to be taxed, under Section 22 (a) of the Internal Revenue Code, upon one-half of the partnership income for each of the taxable years. This conclusion was affirmed by the Circuit Court of Appeals.

ARGUMENT

The income tax treatment of family partnerships was recently before this Court in *Commissioner* v. *Tower,* No. 317, last Term, and *Lusthaus* v. *Commissioner,* No. 263, last Term, both decided February 25, 1946. In factual detail this case is almost identical with the *Tower* case and the court below adhered to the principles that properly govern the decision under this Court's opinions in these two cases.

The Tax Court's opinion carefully analyzes the facts and demonstrates the unreality of the purported transfers by the husbands to their wives, as well as the unreality of the wives' paper interests in the partnership which ensued. Its conclusions are amply supported by the evidence.

The court below did not, as petitioner suggests, fail to consider the question of the wife's contribution to the capital of the partnership but it accepted the Tax Court's finding, which was sup-

ported by evidence, that the petitioner and Sligh did not relinquish control over the assets of the corporation by their gifts of stock to the wives and the wives did not contribute any property to the partnership. This finding was of itself sufficient to support the conclusion of the Tax Court that the wives were not conducting a business with their husbands as a partnership within the meaning of the federal income tax statutes. In addition, the court below properly accepted as a finding of fact the statement in the Tax Court's opinion (R. 192, 195) to the effect that the gifts were made pursuant to a plan to dissolve the corporation and create a partnership with the wives as partners. *Commissioner* v. *Crescent Leather Co.*, 40 F. 2d 833 (C. C. A. 1st); *Insurance & Title Guarantee Co.* v. *Commissioner*, 36 F. 2d 842 (C. C. A. 2d), certiorari denied, 281 U. S. 748; *Sheppard & Myers, Inc.* v. *Commissioner*, 45 F. 2d 50 (C. C. A. 3d), certiorari denied, 282 U. S. 902; *Flynn* v. *Commissioner*, 77 F. 2d 180 (C. C. A. 5th); *American Box Shook Export Association* v. *Commissioner*, decided by the Ninth Circuit June 27, 1946 (1946 C. C. H., par. 9314); *Emerald Oil Co.* v. *Commissioner*, 72 F. 2d 681 (C. C. A. 10th).

The decision of the lower court is correct. The petitioner urges no reasons for granting the writ that would justify a review by this Court under its rules.

CONCLUSION

It is respectfully submitted that the petition for a writ of certiorari should be denied.

J. HOWARD MCGRATH,
Solicitor General.
DOUGLAS W. MCGREGOR,
Assistant Attorney General.
SEWALL KEY,
HELEN R. CARLOSS,
HAROLD C. WILKENFELD,
Special Assistants to the Attorney General.

AUGUST, 1946.

U. S. GOVERNMENT PRINTING OFFICE: 1946